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STATE PASS FEDERAL RESERVE SAN FRANCISCO TCURRAN
USDOC FOR 4430/MAC/EAP/J.BAKER
TREASURY FOR OASIA AND IRS
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TAGS: [ECON](#) [EFIN](#) [EINV](#) [MY](#)
SUBJECT: Malaysia Economic Update June 2007

11. (U) Summary:

- Malaysian Cabinet approves Intellectual Property Courts
- New Islamic Bond thirteen times oversubscribed
- Oil palm prices more than double in past two years
- KL Mayor blames "uncontrolled development" for flash flood damages.

End Summary.

Greenlight for Intellectual Property Courts

12. (U) The Cabinet recently approved Intellectual Property (IP) courts to be set up in all states, according to press reports. Fifteen Sessions Courts will handle criminal intellectual property cases. In addition, the Federal Territory of Kuala Lumpur and the five states with the highest rate of IP infractions -- Selangor, Johor, Perak, Sabah and Sarawak -- each will have one of their High Courts "specially designated" for IP cases. The courts will handle cases under the Trade Description Act 1972, Patent Act 1983, Copyright Act 1987, and Optical Disc Act 2000.

13. (U) Minister of Domestic Trade and Consumer Affairs Shafie Apdal told the press that, as of June 30, the magistrate court had a backlog of 515 IP-related cases, while the Sessions Court's backlog was 1,030 cases. One local law firm told Econoff that IP cases generally take five to eight years, with more complex patent infringement cases taking ten to fifteen years.

14. (SBU) Comment: In April, USTR announced that Malaysia would remain on the Special 301 Watch List this year. Since then, senior Malaysian officials have approached us repeatedly to ask what would be required to improve their ranking. The GOM undoubtedly will expect that the new courts will be taken into account when their 301 status comes up for review.

Overwhelming Demand for New Islamic Bond

¶5. (U) On June 27, Malaysia's state-owned investment fund Khazanah Nasional issued \$850 million worth of convertible sukuk, an Islamic bond that can be exchanged for shares of PLUS Expressways, Malaysia's toll road operator. It offers a fixed 2% "periodic payment" (coupon). Khazanah and its three book runners CIMB, Deutsche Bank and JPMorgan spent 4 days traveling the Middle East on a road show to promote the sukuk among investors there. When Khazanah opened the bookbuilding, it was oversubscribed 13 times. The huge demand prompted Khazanah to increase the offer by 42% to \$850 million from the original \$600 million. Investors from the Middle East purchased 50% of the offer.

¶6. (U) Khazanah owns 66% of PLUS Expressways. If fully exchanged, the bond issue will account for 15% of the company.

¶7. (U) This is only the second Sharia-compliant convertible bond offered by an Asian issuer. Malaysia's first sukuk, issued in September 2006, was convertible into the national telecommunication company, Telekom Malaysia. It offered 1.25% periodic payments.

¶8. (U) The yield to maturity (or "yield to scheduled dissolution" in Islamic terms) was fixed at 90 basis points below the five year US dollar swap rate, giving it a yield of 4.58%.

¶9. (U) A sukuk avoids paying interest, forbidden under the rules of Islamic finance, by creating a dividend-based fund from which periodic payments are made at a fixed rate, in this case 2%. The periodic payments are not guaranteed. PLUS Expressways currently plays a dividend of approximately 4%. The balance will be put into a sinking fund for future annual payments to the bond holders.

KL Flash Floods Cost Millions

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¶10. (U) Kuala Lumpur-Selangor Indian Chamber of Commerce Vice President Ramesh Kadammal estimated in a television interview that damage from flash floods that hit downtown Kuala Lumpur on June 10 amounted to RM 50 million (about US\$ 15 million). Particularly hard hit were the small businesses of the "Little India" and nearby Dang Wangi shopping districts in Kuala Lumpur, where trash clogged the area's already insufficient drainage system. Kadammal said several shop owners had written to Kuala Lumpur City Hall requesting compensation, but had not received a response. ECON FSN visited the area nearly a week later to find that some shopkeepers were still cleaning up.

What Went Wrong?

¶11. (U) In another televised interview, Kuala Lumpur Mayor Hakim blamed "uncontrolled development" both within the city limits and in the surrounding suburbs for the severity of the flooding. He said erosion had decreased the depth of the Klang River that runs through the center of KL. A TV journalist-environmentalist Dr. Karam pointed out that fewer green areas in and around the city resulted in larger volumes of runoff, and that current laws requiring monitoring and environmental protection have not been effective. He called for an integrated approach to city planning, saying the Departments of Drainage and Irrigation, Meteorology, and Public Works must work together with local councils and be held accountable.

"Smart" Tunnel: Will it be as Smart as it Looks?

¶12. (U) Drainage and Irrigation Department Director General Keizrul predicted the RM 2.1 billion (US\$ 618 million) "Smart Tunnel" will solve part of the city's storm drainage problems. The new three-level tunnel under one of KL's most congested highways uses

the bottom level for storm water drainage, directing runoff into retention ponds before dispersing it into rivers downstream of the center of town. The upper levels of the Smart Tunnel opened for auto traffic May 1; however, the bottom level was not operative in time to assist with the June 10 flash floods. The Smart Tunnel has yet to be put to the test.

Palm Oil Price Reaches Record High

¶13. (U) Malaysian oil palm plantation owners and investors are a happy group these days as palm oil prices continue to rise. Crude palm oil prices averaged between RM 2,300 (US\$ 667) and RM 2,450 (US\$ 710) per metric ton over the past several months reaching a peak of RM 2,700 (US\$ 782) in June. Average crude palm oil prices were RM893 (US\$ 235) per metric ton in 2001 and RM 1,389 (US\$ 365) in 2005. Analysts estimate the current cost of production of palm oil to be about RM 800 (US\$ 232) per metric ton. Ignoring processing and marketing costs, this suggests a gross profit margin of over 200%.

¶14. Malaysia currently is the world's largest palm oil producer, but Indonesia, a close second, continues to convert more and more land to oil palm plantations. Many Malaysian plantation companies are participating in the Indonesian expansion. Palm oil and palm oil-based products represent about 5.8% of Malaysia's total export earnings. The U.S. was the fourth largest buyer of Malaysia's palm oil in 2006 (up from tenth place in 2003) after the U.S. Government mandated display of saturated fat or trans fat levels on nutritional labels in January 2006. China is Malaysia's largest palm oil customer, buying nearly a fifth of Malaysia's palm oil exports every year.